

CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 252

October 30, 1959

1959 STATUTORY AMENDMENTS – EFFECT ON 1959 TAXABLE YEAR PARTNER OR BENEFICIARY RECEIVING INCOME FROM A PARTNERSHIP OR TRUST FOR TAXABLE YEARS BEGINNING PRIOR TO 1959

Syllabus:

(1) The 1959 tax rates apply to:

(a) a partner's distributive share of partnership income includible on his return for any period beginning after 12/31/58

(b) a beneficiary's distributive share of trust income includible on his return for any period beginning after 12/31/58

(2) The 1959 capital gains amendments apply to capital gains included in the income received in (1)(a) and (1)(b) above regardless of the amount of time the property was held and even though the partnership or trust sold the property prior to January 1, 1959.

(3) The 1959 capital gains amendments apply to payments received in 1959 from installment sales made in prior years.

General - All provisions of Ch. 830, Stats. 1959, (A.B. 1177) affecting changes in the computation of taxes apply to taxable years beginning after December 31, 1958. (Section 17034). Changes in rates and capital gains treatment are changes in the computation of taxes. (Stats. 1953, Chapter 1640, Sec. 6).

(1)(a) Rates – Partner. -- The partner is required to include in his 1959 income his distributive share of partnership income for the year ended June 30, 1959. Section 17861. This is taxed at the 1959 rates since it is part of the partner's income for such calendar year. I.T. 2837 CB XIII-2 p. 39.

(1)(b) Rates – Beneficiaries. -- Under the same reasoning the 1959 rates also apply to the beneficiary under the same circumstances. Sections 17752(c) and 17764. G.C.M. 5735 VIII-1 p. 203.

(2)(a) Capital Gains – Partner. -- The Internal Revenue Code of 1939 requires a partnership to segregate its capital gain from its other income (Section 183) and the partner to segregate his long term and short term capital gains received from the partnership. (Section 182).

The purpose of these segregations was to enable the partner to offset his capital gains and losses from the partnership against his personal capital gains and losses. Claire Giannini Hoffman, 2 TC 1160 (1943).

A partnership is therefore merely a conduit and the capital gains of the partnership are part of the income of the partner, taxable to him under the law applicable to his taxable year. (Regulations 103, Sec. 19.182-1 as amended by T.D. 5217 January 19, 1943). The Internal Revenue Code of 1954 continues this conduit treatment. (Sections 702, 703). The Personal Income Tax Law (Sections 17852, 17853 and 17854) is substantially the same as the 1954 Code.

(2)(b) Capital Gains -- Beneficiary. The 1959 amendments are applicable to capital gain distributions from a trust under the same reasoning as was used in the case of partnerships. The 1939 and 1954 Internal Revenue Codes as well as California Law all provide that where there is a distribution of capital gain by a trust to a beneficiary the income retains the same character in the hands of the beneficiary as it has in the hands of the trust. Section 17763. Under such circumstances the trust is again a mere conduit and the beneficiary must consider the gain or loss as having been received directly by him, and reportable in accordance with the law applicable to his taxable year.

(3) Installment and Cost Recovery Transactions. -- Income is not realized from transactions reported by either of these methods until the year payment is received. The taxpayer takes the risk that the law will not be changed to his detriment if he defers the realization of income. Snell v. Commissioner, 97 Fed. 2d 891, (5th Cir., 1958). If the capital gains treatment is changed, the law applicable to the year of payment is the proper law to use. Harry B. Golden, 47 BTA 94 (1942). (Regulation 17531-17533(e) of the 1953 regulations.)